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SUBJECT: RRT ERBIL: KRG OIL LINKS TO IRAQI PIPELINE

REF: BAGHDAD 1446

This is an Erbil Regional Reconstruction Team (RRT) cable

¶1. (SBU) Summary: At a June 1 gala event, Presidents Talabani and Barzani officially "turned on" pipelines from Tawke and Taq Taq fields in the Kurdistan Region, which will together add 100,000 barrels a day (bbl/d) through the Iraq-Turkey Pipeline to the Turkish Mediterranean port of Ceyhan. President Talabani also pronounced the Kurdistan Regional Government's (KRG) Production Sharing Contracts (PSCs) "constitutional and legal." CEOs from PSC holders DNO (Norway), Addax (Canada) and Genel Enerji (Turkey) praised the KRG's cooperation and expressed their commitment to expanding work in the region - "the last remaining true oil frontier," according to Addax CEO Jean Claude Gandur. Pressed by the media on how the companies will actually be paid (given the Government of Iraq's continued insistence that these contracts are illegal), KRG officials reiterated that the oil was for the benefit of the Iraqi population, and that the issue would be resolved eventually. Behind the heady mix of self-congratulation and noble-minded pronouncements (and despite the many unresolved issues between the KRG and the GoI), the event was a significant moment for the Kurdistan Region in its coming of age as an oil producing region. End Summary.

"A New Source of Oil for the West"

¶2. (U) Proclaiming Kurdistan Region petroleum "a new source of oil for the West," Kurdistan Regional Government (KRG) Ministry of Natural Resources Senior Adviser Khaled Saleh kicked off a gala event on June 1 to mark the addition of Kurdistan Region oil to the Iraq Turkey Pipeline. Presidents Talabani and Barzani, in a rare joint public appearance, officially "turned on" the pipelines together. Oil will flow from two sources: 60,000 barrels a day (bbl/d) from a trunk line connecting DNO's Tawke field directly to the Iraqi pipeline, and 40,000 bbl/d by truck from Taq Taq field to the K-1 pumping station in Kirkuk. (Note: A few weeks could be required for these levels to be reached. End note.)

¶3. (U) The event, complete with razzle-dazzle light shows, a levitating stand-in oil pump, Star-Wars sound systems, multiple-screen video feeds and bespangled Kurdish folk dancers, took place in the state-of-the art Sami Abdelrahman Conference Center in Erbil. Genel Enerji (which reportedly bankrolled the roll-out) presented a small sample of Kurdistan Region oil encased in lucite to the guests, drawn from a who's who of the Kurdistan Region, the local diplomatic corps, and including visiting Norwegians, Canadians and Turks (representing companies DNO, Addax and Genel Enerji).

From Victim to Victor

14. (U) The carefully choreographed presentations and speeches started on a somber note, with a short video recalling the horrors of the Anfal campaign and showing victims of chemical attacks. Oil was described as a "weapon" which had once been used by Saddam Hussein to buy arms to use against the Kurds. The video then charted the rapid succession of events from the Kurdistan Region's 2007 passage of oil and gas legislation to the conclusion of PSCs with thirty companies from fifteen countries and concluding with the 100,000 bbl/d ready to flow into the national coffers. Other than a brief clip of Oil Minister Shahrastani denouncing the KRG PSCs as illegal, the video did not dwell on disagreements with Baghdad over hydrocarbons management or revenue sharing. QBaghdad over hydrocarbons management or revenue sharing.

CEOS looking happy -- are my stocks rising yet?

15. (U) DNO (Norway) CEO Helge Eide pointed out that only five years had passed since the signing of the PSC - "not a long time in the oil business." He recalled that DNO had been ready to start exporting two years ago, and had "patiently waited for the KRG to make its decision." DNO had no intention of resting on its laurels, and would continue with a goal of reaching 100,000 bbl/d at Tawke and continuing work at new fields in the Erbil license area where early stage production was expected to start in 2010. Addax (Canada) CEO Jean Claude Gandur reported that the "KRG's legal and regulatory systems had fashioned a vibrant upstream oil industry"; four years ago he would have been hard pressed to anticipate how fast and efficiently work would proceed. The 45,000 bbl/d at Taq Taq was described as "a stunning result

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to anyone in the oil world." He called the Kurdistan Region "the last remaining true oil frontier" and one that would attract serious players from the global oil industry.

Genel Enerji Lauds Turkish/Kurdistan Region Ties

16. (U) Genel Enerji CEO Mehmet Sepil praised the "original vision of Mam Jalal Talabani and Barham Saleh" (who had signed the original Taq Taq agreement for the PUK Government in Sulaimaniyah before it was renegotiated by the KRG government 2004) and the full "confidence of the KRG in Turkish entrepreneurship." He noted that Genel Enerji's work in the Kurdistan Region was the first time a Turkish independent producer had worked on a reservoir of this size. Like his Norwegian counterpart, Sepil lamented the fact that it had taken so long to export the oil; "if we had been able to export two years ago, we could have sent out billions of dollars of oil." Sepil explained that Genel Enerji was expanding its activities in the region in what he termed a "life-long partnership" which would also "strengthen political cooperation in the region" and "add value to the Turkish economy." He noted that Genel Enerji would also be investing \$1.1 billion in new infrastructure projects to benefit the Kurdistan region, projects that would be "transparent" and consistent with Genel Enerji's good corporate citizenship standards.

KRG Speakers Stress Benefits to All Iraqis

17. (U) KRG Minister of Natural Resources Ashti Hawrami opened his statement by praising the Federal Constitution which had "laid the foundation for achievements of today" and "witnessed the end of decades of discrimination." Events had shown that oil was not a curse - rather, it could be a source of prosperity and stability. More importantly, today the KR showed the world that "competition and market driven policies could revive the economy of Iraq." He called on "friends in Baghdad" to engage in a fair and strategic policy for hydrocarbons. He committed to continuing to work

transparently and efficiently. Exports would increase by 100,000 bbl/d after June 1. Within a year he promised that KR's total crude oil exports would rise to 250,000 bbl/d within a year, to 450,000 bbl/d by 2010 and to a million bbl/d by 2013. This would eventually increase Iraq's overall exports by 50 percent and, at today's oil prices, increase the Iraqi budget by \$2 billion in one year, by \$5 billion by 2010, and by \$20 billion within four years. Stressing that "our intention is to maximize the benefits for all Iraqis" Minister Hawrami mentioned that the KRG was also planning a strategic gas pipeline (reftel) which would generate even more revenue.

...But Policies Need to Change

¶8. (U) Minister Hawrami cautioned, however, that that "if Federal oil policies did not change to increase production and if fair and transparent revenue sharing law is not passed soon, the consequences will be very serious." Lack of cooperation, according to him, had thus far cost Iraqis \$10 billion. "This must not be repeated." Policies that maximized revenues needed to be put in place. By example, he stated that the cost of Taq Taq - a field with an 180,000 b/d potential - had been under \$500 million. Investors had the incentive to move fast and efficiently. In the rest of Iraq, by comparison, investors were rewarded for having higher costs, rather than for stepping up production. Minister Qcosts, rather than for stepping up production. Minister Hawrami reiterated that the KRG was committed to the principle that revenues were for all of the Iraqi people, and that Article 115 of the Constitution empowered the region to manage all new oil and gas resources. (Note: Inter alia, Article 115 states: "All powers not stipulated in the exclusive powers of the federal government belong to the authorities of the regions and governorates that are not organized in a region." End note.)

¶9. (U) Minister Hawrami also observed that there had been doubts that investors would come; doubts that oil could be exported; and doubts that the companies would get paid. So far two of those had been accomplished. As for the third, (turning away from his prepared statement) Hawrami simply stated (with a grin) "oil talks money. We will get paid." In closing, the Minister highlighted the relationship with Turkey, "with whom the KR was entering a new era of friendship."

¶10. (U) Prime Minister Barzani stated that the KRG was

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contributing to a better and more stable Iraq. Oil investors must be rewarded according to their entitlements. He also stated "we want justice for the people of Kirkuk and the disputed territories" and the "right of return" as promised in the Constitution. The Prime Minister regretted the fact that the KRG's budget allocation was stalled in Baghdad, and noted that if a revenue sharing law was in place, this would not be the case. So long as it was a "budget allocation," it would be subject to delays and political pressures.

President Talabani Declares PSCs Constitutional

¶11. (U) President Talabani took the floor to "reaffirm the constitutionality and legality of the KRG contracts according to Article 112 (d) of the Constitution." Furthermore, he stated, these contracts were in the best interests of the Iraqi people. (Note: Applause greeted both of these statements. End note.) The last speaker, KRG President Masoud Barzani, summed up the event by stating that the Region was showing "by deeds, not words" that revenues belong to all the people of Iraq. "We will continue with this policy." He also took the opportunity to congratulate the PUK on its 31st anniversary, and reaffirm the KDP/PUK coalition.

But the Press is Skeptical

¶12. (U) At a press conference before the opening, foreign media pressed hard on the question of how the companies would actually be paid. Senior Adviser Khaled Saleh fielded the questions, and reiterated that a mechanism would be found and the issue would be resolved soon, but left reporters with more questions than answers.

Comment

¶13. (SBU) Behind the heady mix of self-congratulation and noble-minded pronouncements, the event did indeed mark a significant moment for the Kurdistan Region. Exploitation of the region's impressive natural resource endowment and shaking off the mantle of victimization and poverty will be part of a new discourse and sense of identity in the region. This will, in turn, create new expectations on the part of citizens - expectations for higher standards of living, but also expectations that their leadership will move to resolve the many outstanding issues with Baghdad. The KRG leadership is banking that its concrete achievement and contribution to central government coffers will encourage an equal degree of flexibility on the part of the GOI.

HILL